

REBUTTAL TESTIMONY
OF
DAVID SACKETT
Economic Analyst
Policy Program
Energy Division
Illinois Commerce Commission

Northern Illinois Gas Company
d/b/a Nicor Gas Company

Petition for an order re-approving an agreement for the provision of facilities and services and the transfer of assets between Nicor Gas Company and Nicor Inc. and its subsidiaries

Docket No. 09-0301

December 2, 2010

PUBLIC VERSION (Denoted by Gray Highlight)

Table of Contents

I.	WITNESS QUALIFICATIONS	1
I.	PURPOSE OF TESTIMONY AND BACKGROUND INFORMATION.....	1
II.	SUMMARY OF RECOMMENDATIONS	3
III.	OPERATING AGREEMENT STRUCTURE.....	4
	ISSUES/CONCERNS	4
	1. <i>Balance of the interests of ratepayers and Nicor Inc.'s shareholders under Nicor Gas' OA.</i>	5
	2. <i>Nicor Gas' decision makers' direct and indirect incentives to make affiliates profitable.</i>	6
	3. <i>Nicor Inc. is not indifferent to profits from Nicor Gas or an unregulated subsidiary.</i>	9
	4. <i>Nicor Gas' actions under the OA's "umbrella-type" structure.</i>	12
	OPERATING AGREEMENT STRUCTURE CONCLUSIONS AND RECOMMENDATIONS.....	12
IV.	GAS LINE COMFORT GUARD	13
	ISSUES/CONCERNS	14
	1. <i>Commission authority to regulate Local Distribution Company ("LDC") support of affiliate products.</i>	14
	2. <i>GLCG and incremental safety benefits.</i>	21
	3. <i>The market competitiveness of gas line warranty products in Nicor Gas' service territory.</i>	33
	4. <i>Nicor Gas' Cost Support for GLCG.</i>	60
	GLCG CONCLUSIONS AND RECOMMENDATIONS	64
V.	WEBSITE	66
	ISSUES/CONCERNS	66
	1. <i>Nicor Gas' webpages and Commission Jurisdiction.</i>	66
	2. <i>Solicitation by potential competitors on Nicor Inc.'s website.</i>	67
	WEBSITE CONCLUSIONS AND RECOMMENDATIONS	68
VI.	BILLING SERVICES	69
	ISSUES/CONCERNS	69
	BILLING SERVICES CONCLUSIONS AND RECOMMENDATIONS	77

Figure 1 - List of Attachments	2
Figure 2 – Repairs done for all customers	26
Figure 3 – GLCG Actuarial Cost and Risk Premium.....	34
Figure 4 – Risk Premium Comparison	42
Figure 5 – Corrections to Staff Ex. 2.0 Numerical Analysis	62

1 **I. Witness Qualifications**

2 **Q. State your name and business address.**

3 A. David Sackett, Illinois Commerce Commission, 527 East Capitol Avenue,
4 Springfield, Illinois, 62701.

5

6 **Q. Are you the same David Sackett who previously testified in this proceeding?**

7 A. Yes.

8

9 **I. Purpose of Testimony and Background Information**

10 **Q. What is the subject matter of your rebuttal testimony?**

11 A. This testimony responds to the rebuttal testimonies of certain witnesses for
12 Northern Illinois Gas Company d/b/a Nicor Gas Company (“Nicor Gas” or
13 “Company”) offered in support of its petition for an order re-approving an
14 agreement for the provision of facilities and services and the transfer of assets
15 between Nicor Gas and Nicor Inc. and its subsidiaries. In particular, I respond to
16 the rebuttal testimonies of Nicor Gas witnesses Mr. Gerald P. O’Connor, Mr.
17 John Erickson and Dr. Agustin J. Ros regarding Nicor Gas’ Operating Agreement
18 (“OA”), the Gas Line Comfort Guard (“GLCG”) product offered by its affiliate
19 Nicor Services, Nicor Gas’ call center, website hosting, and the third party billing
20 service that Nicor Gas offers to parties offering products to its ratepayers. I

briefly address the direct testimony of intervenor witnesses Mr. David J. Effron for the Attorney General and the Citizen's Utility Board ("AG/CUB") and Mr. James L. Crist for Dominion Retail Inc.

Q. Do you have any attachments to your testimony?

A. Yes. I have attached the following to my rebuttal testimony.

Att.	Source
A	Nicor Inc.'s 2010 Proxy Statement
B	Strobel SEC Form 4 November 2, 2010
C	O'Connor SEC Form 4 November 2, 2010
D	Nicor Gas response to Staff DR DAS 19.12 Exhibit 1
E	Nicor Gas response to Staff DR DAS 11.06 Corrected Exhibit 1
F	Nicor Gas response to Intervenor DR IGS 2.19 Exhibit1
G	Nicor Gas inspection proof from website
H	Nicor Gas' 2010 Safety Notice
I	SES responses to Staff DR DAS-SES 1.01-1.05
J	IGS responses to Staff DR DAS-IGS 1.01-1.05
K	Nicor Gas and Manchester Group correspondence regarding Utility Shield
L	Nicor Gas response to Staff DR DAS 17.06 Corrected Exhibits 1 and 2
M	Nicor Gas Consolidated Billing Services Agreement
N	Nicor Gas response to Staff DR DAS 18.17
O	Nicor Gas corrected response to Staff DR DAS 3.03 Corrected Exhibit 1
P	Nicor Gas response to Staff DR DAS 16.03
Q	Nicor Gas response to Intervenor DR IGS 2.18 Exhibit 2
R	Nicor Gas response to Staff DR DLH 2.02 Exhibit 13 Corrected Exhibit A
S	Nicor Gas response to Staff DR DAS 10.13
T	Nicor Services Billing Service Cost Studies
U	Third Party Billing Service Cost Studies

Figure 1 - List of Attachments

29 **II. Summary of Recommendations**

30 **Q. Please summarize your recommendations.**

31 A. I have the following recommendations for the Commission. Recommendations 1
32 through 7 are the same as in my direct testimony and Recommendation 8 is new
33 in rebuttal. I also clarify my support for Ms. Hathhorn's pricing recommendations
34 as stated below:

35 **Recommendation 1:** Change Nicor Gas' OA to require Commission approval of
36 any sub-agreement, as defined in Staff Ex. 3.0, Attachment A, *prior* to it becoming
37 effective.

38 **Recommendation 2:** Change Nicor Gas' OA to preclude customer solicitation.

39 **Recommendation 3:** Require Nicor Gas to provide factual information regarding its
40 currently available repair services.

41 **Recommendation 4:** Change Nicor Gas' OA to preclude operational services other
42 than those specifically authorized.

43 **Recommendation 5:** Change Nicor Gas' OA to require that any Nicor Gas service,
44 excluding "corporate support," that supports any affiliate product that is offered to
45 Nicor Gas customers be provided to non-affiliates on a non-discriminatory basis.

46 **Recommendation 6:** Change Nicor Gas' OA to preclude website hosting of Nicor
47 Gas by any affiliate.

Recommendation 7: Require Nicor Gas to charge any affiliate the same charge as other third parties under the Third Party Billing Service.

Recommendation 8: Require Nicor Gas to allow any Customer Select supplier to include non-commodity charges under the Third Party Billing Service.

Further, I support Staff witness Hathhorn's pricing recommendations (Recommendations 1-3, Staff Exs. 1.0 and 3.0).

III. Operating Agreement Structure

Issues/Concerns

Q. What concerns did you raise in your direct testimony with the OA as it exists currently?

A. Nicor Gas argued that its OA is in the public interest, because its ratepayers financially benefit since the revenues from the services offset fixed costs that they would otherwise have to pay. (Nicor Gas Ex. 1.0, pp. 12, 14) One concern was that Nicor Gas' criteria for what is in the public interest is too narrow, because it did not net its alleged financial benefit against the financial harm done to those ratepayers who purchase affiliate products that are not subject to competitive pressures. My second concern was that the agreement is open to potential abuse, because it is an "umbrella-type" agreement meaning that the Commission approves the umbrella (OA) but then has no pre-approval on subsequent agreements.

68

69 **Q. How did Nicor Gas respond to your concerns?**

70 A. Nicor Gas argued that an OA is intended to eliminate extra unnecessary
71 proceedings and create efficiency for the ICC and Nicor Gas. Nicor Gas witness
72 O'Connor noted that the OA has been in effect for 10 years, balancing the interests
73 of ratepayers and Nicor Gas. "Agreements like the current one balance the
74 interests of ratepayers and the utilities, and promote administrative efficiency for the
75 Commission." (Nicor Gas Ex. 2.0, pp. 9-10)

76

77 **1. Balance of the interests of ratepayers and Nicor Inc.'s shareholders under**
78 **Nicor Gas' OA.**

79 **Q. Does Nicor Gas' OA "fairly balance the interests of ratepayer and the**
80 **Company"?**

81 A. No. Nicor Gas witness O'Connor states "Nicor Gas' existing, Commission-
82 approved Agreement is reasonable, in the public interest, and fairly balances the
83 interests of ratepayers and the Company." (Nicor Gas Ex. 2.0, p. 2) However, the
84 evidence presented by myself and Staff witness Hathhorn shows that the benefits,
85 while shared to some degree, are not "fairly balanced." The benefits accruing to
86 the Company and Nicor Inc.'s shareholders are unfairly higher than those accruing
87 to ratepayers. A clear example is the solicitation to potential customers that Nicor

Gas provides at cost exclusively to its affiliate, Nicor Services. This service is extremely valuable, since it gives Nicor Services the first pass at all prospective new customers, but Nicor Services only compensates Nicor Gas for its Fully Distributed Cost (“FDC”). While this service enables Nicor Services to earn millions of dollars annually, it pays less than \$200,000 to Nicor Gas for this privilege. (Staff Ex. 2.0, pp. 58-62)

Q. Nicor Gas witness O'Connor characterizes Staff's recommended prevailing price definition as “a solution in search of a problem.” (Nicor Gas Ex. 2.0, pp. 14-15, lines 309-311) Do you agree that there is no evidence of a need for a change to this part of the OA?

A. No. The evidence about solicitation for affiliate products demonstrates that Nicor Gas ratepayers are not receiving adequate compensation for the *value* of the services that Nicor Gas is providing for Nicor Services. Staff witness Hathhorn's Recommendations 1, 2, and 3 correct some of that discrepancy. My recommendations complete the correction for the discrepancy.

2. Nicor Gas' decision makers' direct and indirect incentives to make affiliates profitable.

Q. Do you think that Nicor Gas is acting in the best interest of its ratepayers

with respect to the OA?

A. No. Nicor Gas is not acting in the best interest of its ratepayers. Nicor Gas is acting in the best interest of Nicor Inc.'s shareholders. Any departure from this is the exception, not the rule. Nicor Gas decision makers' remuneration is tied to their making decisions in the best interest of Nicor Inc.'s shareholders. According to Nicor Inc.'s 2010 Proxy Statement (Attachment A), Nicor Gas' decision makers, that is, executives, managers and supervisors, all participate in various incentive plans that seek to align the incentives of the decision makers with the interests of Nicor Inc.'s shareholders. Thus, these plans are primarily tied to the performance of Nicor Inc. and its stock. Nicor Gas' response to Staff Data Request ("DR") DAS 17.02 Exhibit 2 lists some of those officers who are decision makers for both Nicor Gas and Nicor Inc.

Q. What financial incentives influence Nicor Gas' decision makers with respect to affiliate profits?

A. It is my understanding that there are three financial incentives that encourage shifting profits to affiliates. First, some decision makers are required to own significant amounts of Nicor Inc. stock. "Nicor requires that all officers acquire and retain Nicor's Common Stock and stock equivalents at least equal in value to certain ownership levels....Currently, all NEOs have met their ownership

requirements.” These ownership levels are at least 1 times their base salaries for all senior officers. (Attachment A, p. 22) For example, based on SEC Form 4s filed on November 2, 2010 (Attachments B and C, respectively), CEO Russ M. Strobel has more than \$3.8 million in Nicor Inc. stock while Senior Vice President (and Nicor Gas witness in this case) Gerald P. O'Connor has more than \$500,000 in Nicor Inc. stock. As a result of such stock ownership, all officers benefit from an increase in Nicor Inc.'s stock price. Second, these officers benefit from dividends. Finally, many decision makers receive incentive compensation that is linked to the financial performance of Nicor Inc. rather than Nicor Gas directly. For example, in 2009, Mr. Strobel made an additional \$2.5 million over his base salary of \$750,000, as a result of incentive compensation. (Attachment A, p. 23)

Q. Do Nicor Gas' decision makers have a fiduciary responsibility to Nicor Inc.'s shareholders?

A. Yes. Since Nicor Gas is wholly owned by Nicor Inc., its decision makers are ultimately responsible to Nicor Inc.'s shareholders. Certainly there is nothing wrong with this arrangement but the consequence is that it cannot be assumed that these decision makers will do what is best for the ratepayers. Outside forces, such as the Commission, must impose restraints on decision makers. Rate regulation performs

148 this basic function on much of the utility's actions. However, the action by affiliates
149 that occurs apart from regulated business but involves Nicor Gas bears greater
150 scrutiny.

151
152 **Q. How does the profitability of GLCG and affiliates negatively affect**
153 **ratepayers?**

154 A. When Nicor Services provides a product to Nicor Gas customers through Nicor
155 Gas' facilitation and solicitation efforts on behalf of that product, Nicor Gas'
156 decision makers profit when the affiliate profits. When other parties want to offer
157 similar products which would compete with an affiliate product and Nicor Gas
158 effectively prevents the provision of similar competitive and equivalent products,
159 Nicor Gas is essentially creating monopoly power for products such as GLCG.
160 As Nicor Gas overprices GLCG, decision makers and affiliates profit while
161 ratepayers are harmed.

162
163 **3. Nicor Inc. is not indifferent to profits from Nicor Gas or an unregulated**
164 **subsidiary.**

165 **Q. Nicor Gas witness Dr. Ros maintains that Nicor Inc. is indifferent to profits**
166 **between its subsidiaries. Do you agree?**

167 A. No. Dr. Ros states, “Nicor Gas does not have an incentive to provide a subsidy to
168 Nicor Services because the GLCG product is provided in a competitive marketplace
169 and Nicor Services cannot price above the competitive level. Thus, the loss that
170 Nicor Gas would incur from providing a subsidy could not be recovered through the
171 GLCG product.” (Nicor Gas Ex. 4.0, p. 11) I have two comments. First, I strongly
172 disagree with his assertion that GLCG is provided in a competitive market. Second,
173 even if GLGC were provided in a competitive market there would be an incentive
174 for Nicor Gas to subsidize GLGC to lower its costs to create an economic profit at
175 the competitive price.

176

177 **Q. Why do you disagree with his assertion that GLCG is provided in a**
178 **competitive market?**

179 A. I provide extensive evidence below showing that the price of GLCG is above the
180 competitive level. Specifically, I show that Nicor Services possesses a dominant
181 market share, has exclusive access to three significant Nicor Gas provided services

and enjoys a significant mark up over the actuarial cost¹ of GLGC. Thus, I conclude that the market for gas line warranty products is not competitive in Nicor Gas' service territory and as such, GLGC is not priced in a competitive market.

Q. Even if GLGC were provided in a competitive market and price, why would Nicor Gas still have an incentive to subsidize GLGC to lower GLGC's costs to create an economic profit?

A. If Nicor Gas provides an input to GLGC at a below market price, and refuses to provide that input to competitors at that same price, it can create profits for GLGC even without Nicor Services having the ability to raise the price. Nicor Gas can provide the subsidy due to the below market price input being provided to GLGC, and the reduction in its revenues below what would occur had a market price been charged covered by its customers. Nicor Gas admits that in a test year, Nicor Gas' repair costs offset repair revenues. (Nicor Gas response to Staff DR DAS 17.07) If

¹ Actuarial cost is the cost that will occur given the law of large numbers, the probability of repairs and the cost of those repairs. "The actuarial cost, different than the market price of insurance, is the expected size of the loss multiplied by the probability of the loss." (Nicor Gas response to Staff DR DAS 18.09)

GLCG was offered by Nicor Gas, any revenue from GLCG would offset the revenue requirements. At the same time, when GLCG is offered by Nicor Services, Nicor Services' revenues are not subject to regulation that ties its allowed revenues to its costs. As a result, Nicor Gas has an incentive to subsidize Nicor Services products.

4. Nicor Gas' actions under the OA's "umbrella-type" structure.

Q. Is there evidence that the umbrella nature of the OA harms ratepayers?

A. Yes. Nicor Gas has approved interactions with its affiliate without any Commission review that are not in the best interests of its ratepayers. Specifically, the mover call agreement which allows Nicor Services exclusive marketing access to new Nicor Gas customers significantly benefits Nicor Services, but provides only very limited benefits to Nicor Gas ratepayers. When both Nicor Gas and Nicor Services mislead ratepayers into signing up for GLCG by falsely implying it is required to receive repair services (Staff Ex. 2.0, pp. 21-23), the beneficiary is Nicor Inc.'s shareholders. (Id., pp. 59-61)

Operating Agreement Structure Conclusions and Recommendations

Q. What do you recommend with regard to the structure of the OA?

A. Recommendation 1: Change Nicor Gas' OA to require Commission approval of any sub-agreement as defined in Staff Ex. 3.0, Attachment A, *prior* to it becoming effective. The sub-agreements that I am referring to are those "entered into under the authority of the operating agreement" as provided by Mr. O'Connor in response to Staff DR DLH 2.02. The alternative advocated by Staff witness Hathhorn in her Recommendation #5 to require public disclosure of all sub-agreements should, at a minimum, be adopted.

IV. Gas Line Comfort Guard

Q. Please summarize the testimony regarding Nicor Services' Gas Line Comfort Guard ("GLCG").

A. In my direct testimony, I raised several concerns about GLCG. The GLCG product demonstrates many of the OA's problems. (Staff Ex. 2.0, pp. 35, 46-50) AG/CUB witness Mr. Effron also found that GLCG was overpriced and not in the public interest. (AG/CUB Ex. 1.0, pp. 15-16) Nicor Gas responded to Staff and intervenor testimony by arguing that the Commission lacks the jurisdiction to regulate GLCG. (Nicor Gas Ex. 2.0, pp. 35, 56) Second, Nicor Gas raised safety concerns regarding Staff's recommendations to stop Nicor Gas from performing repairs and inspections for Nicor Services on behalf of GLCG customers. (Nicor Gas Ex. 3.0, pp. 6-21) Third, Nicor Gas claimed that the price of GLCG must be competitive

because of the presence of actual competitors, potential competitors and the presence of self insurance as an option. (Nicor Gas Ex. 4.0, pp. 24-32) Fourth, Nicor Gas attempted to cast doubt on the totality of the cost analysis I provided about GLCG. (Nicor Gas Ex. 2.0, pp. 48-52)

Issues/Concerns

Q. How do you respond to Nicor Gas' rebuttal testimony regarding GLCG?

A. I have four responses:

1. The Commission has authority to regulate Nicor Gas' support of affiliate products.
2. GLCG provides no incremental safety benefits.
3. The market for gas line warranty products in Nicor Gas' service territory is not competitive.
4. Nicor Gas' cost analysis is problematic.

1. Commission authority to regulate Local Distribution Company ("LDC") support of affiliate products.

Q. What did Nicor Gas state regarding the extent of the Commission's authority?

254 A. Nicor Gas witness O'Connor argues that the Commission does not have the
255 authority to regulate the price of GLCG, that the Illinois Department of Insurance
256 ("DOI") already regulates GLCG and that the Illinois American Water case ("IAW
257 case"), Docket No. 02-0517, is not relevant in this case.

258

259 **Q. What did Nicor Gas state regarding the Commission's authority to regulate**
260 **GLCG?**

261 A. Nicor Gas witness O'Connor stated that since GLCG is not subject to
262 Commission regulation, the Commission should not "interfere with product
263 offerings" or assess "the commercial merits or profitability of GLCG." (Nicor Gas
264 Ex. 2.0, p. 56) Furthermore, Nicor Gas witness Dr. Ros stated that it was
265 inefficient for the Commission to regulate prices of affiliate products offered in a
266 competitive market. (Nicor Gas Ex. 4.0, pp. 8-9)

267

268 **Q. Has Staff proposed that the Commission regulate GLCG's price?**

269 A. No. Staff did not advocate that the Commission regulate the price of GLCG.

Rather, Staff proposed that the Commission regulate those services provided by Nicor Gas under the OA's authority that support Nicor Gas' affiliates' products. GLCG pricing provides insight into whether the provision of these services—and, by extension, the OA—is in the public interest.²

Q. Does Nicor Gas argue that the DOI regulated GLCG?

A. Yes. Nicor Gas witness O'Connor stated the DOI already regulates GLCG. Specifically he lists "financial, registration, disclosure and recordkeeping requirements,...contract terms,...the terms the conditions for obtaining service, the existence of deductibles, any limitations and exclusions, cancellation and refund policies and whether failures relating to ordinary wear and tear are covered." (Nicor Gas Ex. 2.0, p. 31) This does not address Staff's concerns, because the regulation of GLCG by the DOI is limited. The DOI only regulates the presence of certain obligations in the terms and conditions and whether they are fulfilled. It does not regulate the product's pricing or whether the provision of

² While Nicor Gas could provide GLCG, which would then place GLCG under Commission regulation, Nicor Gas has chosen not to do so. (Nicor Gas response to Staff DR DAS 1.09)

utility services to support the product is in the public interest.

Q. Does the DOI regulate the relationship between utilities and affiliates who provide warranty or insurance products?

A. No. The services provided by a utility for its affiliates under an operating agreement falls under the jurisdiction of the Commission. DOI regulation does not protect consumers from the extension of Nicor Gas' regulated monopoly power into the market for gas line warranty products. Only the Commission has jurisdiction over what services may be performed under the OA. Only the Commission has the jurisdiction to determine whether the provision of these services is in the public interest.

Q. Please explain how the product from the IAW case, Water Line Protection Plan ("WLPP"), is similar to GLCG?

A. The WLPP was a product offered by an IAW affiliate which would warranty the pipes that were the responsibility of the customer against breakage. This was a seldom used product that used an endorsement from the water company that the Commission feared would result in undeserved profits for the affiliate to the detriment of the ratepayer. The utility failed to provide economic evidence to demonstrate that the product was properly priced. The Commission's concern

was with the potential for ratepayers to be over-charged, as opposed to being more safe.

Q. How did Nicor Gas respond to Staff's testimony regarding the IAW case?

A. Nicor Gas witness O'Connor stated that it was irrelevant, because the facts of that case and the instant case are different. He specifically notes four differences. First, the Nicor Gas OA has been previously deemed to be in the public interest by the Commission. Second, Mr. O'Connor maintains that GLCG has a proven track record with a large number of satisfied customers. Third, he asserts that Nicor Gas has provided an economic basis for GLCG. And fourth, according to Nicor Gas witness Erickson, GLCG serves an important safety function. (Nicor Gas Ex. 2.0, pp. 57-58)

Q. Does prior approval of the OA by the Commission mean that the OA remains in the public interest?

A. No. While I am not a lawyer, it is my understanding that the Commission has the ability to review prior authorizations and approvals of agreements and does so on a regular basis to consider new facts that come to its attention. Nicor Gas' assertion that the Commission has already approved this document and that the last ten years have been beneficial to both ratepayers and Nicor Gas overlooks

the issue. In my opinion, the Commission has ample evidence of affiliate agreements under the OA that are not in the public interest, and it is proper to reevaluate the OA in light of that evidence. The Commission has the authority to change and revise the OA in light of abuses that have occurred, despite having previously approved the OA. The Commission's prior approval of the OA does not mean that the OA would never need reexamining or restructuring. In relying on the OA's prior approval to avoid updates or changes, Nicor Gas is escaping its responsibilities and obligations to its ratepayers. Furthermore, the Commission already considered the fact that the OA needed reexamining when it ordered Nicor Gas to seek re-approval of its OA in the Company's last rate case. (Order, Docket No. 08-0363, March 25, 2009, p. 182)

Q. What is the weight of the economic evidence in the present case?

A. Again while I am not an attorney, the IAW case, which provides germane guidance for this case, makes clear that the utility bears the burden of proof. Nicor Services could have provided Nicor Gas with detailed cost information to support a cost analysis of GLCG and other products. Rather than providing such information here, Nicor Gas has introduced theoretical conjecture about what might happen under certain ideal and unrealistic circumstances. Furthermore, the additional evidence provided in this rebuttal shows even more conclusively

that there is no significant competitive pressure on GLCG's price. And Nicor Gas has consistently acted in its affiliate's best interest to the detriment of its ratepayers. GLCG is not priced in a competitive market and has not been shown to be properly priced nor in the public interest.

Q. Is the IAW case relevant to this proceeding?

A. Yes. As I noted in my direct testimony, the Commission specifically acknowledged that as these types of agreements become more prevalent, the abuses associated with them will be more fully known. (Staff Ex. 2.0, pp. 11-13) Such abuses are precisely what Staff is alleging in the instant case. While certainly not binding, the Commission's rationale in the IAW case is instructive and relevant. The Order on Reopening states,

The Commission acknowledges that *an appropriate analysis could have been done* and is not available for one reason or another, but to simply accept IAWC's assertions that the WLPP is in the public interest *in the face of legitimate questions raised by Staff, CUB, and the AG* would be a disservice to Illinois consumers and an offense to the Commission's obligations under the Act. Accordingly, the Commission finds that the WLPP has not been shown to be in the public interest and will not be approved.
(Order on Reopening, Docket No. 02-0517, September 16, 2003, p. 16, emphasis added)

Q. Does Nicor Gas provide its ratepayers with sufficient information to make

efficient decisions regarding gas line warranty products?

A. No. Nicor Gas does not publicize the fact that it will do repairs if a gas leak is found. GLGC misleads the customers into thinking that GLGC is the only way to prevent shutoffs if a leak is found. As a result, Nicor Inc.'s shareholders benefit from overconsumption of GLCG and ratepayers who purchase GLCG are harmed.

Q. Should the Commission intervene on behalf of consumers?

A. Yes. In addition to my rebuttal of Mr. O'Connor's assertions, I believe the evidence of asymmetric information provided below, which results from Nicor Gas' decision to not publicize its Customer Care Services requires Commission attention. In my opinion, the continued provision of certain services under the OA results in an unwarranted transfer of money from ratepayers to Nicor Inc.'s shareholders. The provision of these services is therefore not in the public interest and should not be authorized under the OA. If the Commission determines that certain services should continue, then it should require Nicor Gas to provide them in a non-discriminatory manner.

2. GLCG and incremental safety benefits.

Q. Nicor Gas witness Erickson argued that Staff is ignoring the safety

389 **considerations with GLCG. Do you agree?**

390 A. No. I do not ignore the effects on safety in my recommendations. His
391 statements reflect his lack of understanding of the incremental comparison that I
392 made.

393

394 **Q. Nicor Gas witness Erickson testifies that GLCG provides an important**
395 **safety function and that Staff's proposal to not permit repairs directly for**
396 **Nicor Services is irresponsible. Do you agree that the relevant comparison**
397 **here is between what Nicor Gas considers a limited legal obligation and the**
398 **services provided under the GLCG program?**

399 A. No. Like Mr. O'Connor, Mr. Erickson mistakenly compares Nicor Gas' position
400 that it is not obligated to provide directly to customers the services it provides in
401 support of GLCG. (Nicor Gas Ex. 3.0, pp.7-8) This comparison is improper
402 because it does not reflect the actual options that the ratepayer faces. The
403 reality of Nicor Gas' own services for ratepayers is the relevant comparison here.

404

405 **Q. Do the repairs and inspections that Nicor Gas performs on Nicor Services'**
406 **behalf provide important safety functions?**

407 A. Certainly. These repairs and inspections provide Nicor Gas ratepayers with
408 services necessary to keep them safe. The danger posed by gas leaks are widely
409 known and not disputed by Staff in this case.

410

411 **Q. What was at issue in Docket No. 05-0341 referenced by Mr. Erickson?**

412 A. In that case, the utility shareholders profited by failing to fulfill its federally-mandated
413 minimum inspections (once every five years) of the utility's *own* pipes on
414 ratepayers' premises. The instant case is a case where utility shareholders profit
415 from the utility's failure to provide information about its repair and inspection
416 services. The two cases are *not* relevant to each other.

417

418 **Q. Nicor Gas witness Erickson states that, "Mr. Sackett says that by his**
419 **calculation only 2% of GLCG customers have submitted claims and that**
420 **many leak repairs are minor." (Nicor Gas Ex. 3.0, p. 18) Did you make this**
421 **statement?**

422 A. No. I stated, "Given that the annual probability occurrence of repairs is less than
423 2% and the average cost per repair is less than \$76, the 'guard' is clearly not worth
424 the annual price of \$59.40." (Staff Ex. 2.0, p. 48) I was referring to the "guard" or
425 "risk premium." I made no such statement that repairs were "minor" in my direct
426 testimony, as acknowledged by Mr. Erickson in his responses to Staff DRs DAS

21.05 and 21.06. In fact, he puts words in my mouth in order to use Staff arguments from Docket No. 05-0341, which might have been appropriate if I had said what he claimed. However, he is wrong in this assertion.

Q. Do you agree that GLCG inspections and repairs serve an *incremental* safety function?

A. No. I do not believe that GLCG repairs and inspections provide a safety function *incremental* to those same services provided by Nicor Gas.

Q. How does Nicor Gas characterize its Customer Care Services?

A. Nicor Gas claims that Staff's request concerning "Nicor Gas' inspection and repair services"

misconstrues the services that Nicor Gas provides....*Nicor Gas states that it does not offer an inspection and repair service.* The Company provides emergency response, turn-on, and turn-off services, the *primary* function of which is to ensure no hazardous or unsafe conditions exist. Once an unsafe or hazardous situation is addressed, at the Company's discretion *the Company may provide incremental repairs at the customer's request.*"

(Nicor Gas responses to Staff DRs DAS 18.01, 19.09, 19.12 (Attachment D) and 19.14, emphases added)

Q. Does Nicor Gas provide repair services to all of its ratepayers equivalent to those it provides under GLCG?

A. Yes. The exact same repairs are available from Nicor Gas without purchasing

GLCG. (Nicor Gas Ex. 2.0, p. 44) The repair services provided under GLCG are actually available to all ratepayers under Nicor Gas' Standard Practice Customer Care Services-1 ("SP CCS-1" or "Customer Care Services") at charges equal to FDC. (Staff Ex. 2.0, Att. I) While these repairs are done subsequent to an emergency response, so are the repairs performed on behalf of Nicor Services under GLCG. The only difference is a financial one – who gets the bill. So the difference is a semantic one.

Q. How many repairs has Nicor Gas performed in the past three years for non-GLCG customers?

A. As shown below in Figure 2 – Repairs done for all customers, Nicor Gas has reported that it has performed over 18,500 repairs for its customers who were not on GLCG during 2007 through 2009. (Nicor Gas response to Staff DR DAS 11.06 Corrected Exhibit 1 – Attachment E)

Count of Non-GLCG Customer Piping Repairs by Cost Category				
Category	2007	2008	2009	Total
\$50 or less	6,025	4,627	3,507	14,159
\$50.01 to \$100	1,808	1,214	881	3,903
\$100.01 to \$200	190	124	107	421
\$200.01 to \$300	10	12	9	31
\$300.01 to \$600	5	4	1	10
\$600.01 to \$1000			2	2
over \$1000.01				0

Total Count	8,038	5,981	4,507	18,526
Count of GLCG Customer Piping Repairs by Cost Category				
Category	2007	2008	2009	Total
\$50 or less	4,683	4,630	3,350	12,663
\$50.01 to \$100	3,685	3,293	3,296	10,274
\$100.01 to \$200	582	566	736	1,884
\$200.01 to \$300	37	49	48	134
\$300.01 to \$600	9	7	3	19
\$600.01 to \$1000	1			1
over \$1000.01				0
Total Count	8,997	8,545	7,433	24,975

Figure 2 – Repairs done for all customers

Q. What is Nicor Gas witness O'Connor's testimony with respect to provision of appliance connector inspection services without a gas leak report?

A. Mr. O'Connor states that Nicor Gas will not "conduct inspections for dangerous connectors absent a report of a leak by the customer." (Nicor Gas Ex. 2.0, p. 45)

Q. Is this an accurate statement?

A. No, this is not true. I have found three indicators that, in fact, Nicor Gas does perform such inspections for its ratepayers absent a report of a gas leak or emergency response.

Q. What evidence is there that Nicor Gas *replaces* appliance connectors?

479 A. The repair services provided under GLCG are actually available to all ratepayers
480 under Nicor Gas' Standard Practice Customer Care Services-1 ("SP CCS-1" or
481 "Customer Care Services"). "Replace appliance connector" is listed under "Charge
482 Services" of the "General Gas Appliance Service." (Staff Ex. 2.0, Att. I, p. 7)
483 Furthermore, Nicor Gas' Field Employees Guidelines provided in response to
484 Intervenor DR IGS 2.19, Exhibit 1 (Attachment F) states, "In keeping with the Brass
485 Connector Policy Nicor Gas has deemed that all brass connectors found at a
486 customer's premise will either be removed, replaced or safely disabled when found
487 by Nicor Gas personnel."

488
489 **Q. What evidence is there that Nicor Gas *inspects* for dangerous appliance**
490 **connectors?**

491 A. First, Nicor Gas' webpage states that such inspections are available from Nicor Gas
492 on its "Find a Qualified Professional" page under its safety information about
493 appliance connectors. "Call Nicor Gas at 1 888 288-8110 to get a quote or

494 *schedule an inspection.*³ Second, in the Frequently Asked Questions section of
495 the same information, the question is posed, “I’ve checked my connectors and
496 know they’re uncoated brass. I only want to schedule a *replacement*.” To answer
497 this question, Nicor Gas states, “In order for Nicor Gas to replace your connectors,
498 *we must conduct the inspection.*”^{4 5}(Attachment G, emphasis added)
499

500 **Q. What other evidence is there that Nicor Gas inspects for dangerous**
501 **appliance connectors?**

502 A. On September 9, 2010, I personally scheduled a Nicor Gas inspection on my home
503 appliance connectors to determine if they were dangerous through the Nicor Gas
504 call center. The person I talked to informed me that such inspections were available
505 from Nicor Gas for \$67. So, “absent a report of a leak” or other emergency
506 response, I scheduled an “inspection for dangerous connectors” for my home on

³ http://www.nicor.com/en_us/residential/safety/find_qual_pro.htm (Attachment G)

⁴ http://www.nicor.com/en_us/residential/safety/connectors_faq.htm (Attachment G)

⁵ It is noteworthy that these are the only public acknowledgments that Nicor Gas provides inspections of appliance connectors; (the website does not mention Nicor Gas’ repair services.

September 17, 2010. This is direct evidence that despite Mr. O'Connor's assertion to the contrary, Nicor Gas will perform such inspections.⁶

Q. What other objections do you have about Mr. O'Connor's statement?

A. If his claim were true, I believe that it is not acceptable that Nicor Gas only provides inspections or repairs to ratepayers who purchase a warranty product from its affiliate; if these services are *essential* to customer safety, then Nicor Gas should provide them at cost to ratepayers. Furthermore, such a distinction between GLCG customers and non-GLCG customers runs counter to the legally mandated disclaimer that "customers are not required to buy products or services from Nicor Services in order to receive the same quality of service from the gas utility."⁷ In my opinion, "quality of service" must include the option to receive safety inspections from Nicor Gas directly.

⁶ Incidentally, the Nicor Gas representative solicited me for GLCG, informing me that I could sign up for GLCG any time before that service was performed and that I could avoid the \$67 fee and that it would be covered under my GLCG plan.

⁷ This notice is required by the HVAC affiliate marketing section of the Public Utility Act. (220 ILCS 5/7-208) Quoted from: http://www.nicorinc.com/en_us/nicor_services/protection_solutions/gas_line.htm

521 **Q. What conclusion do you reach from the fact that Nicor Gas provides to all**
522 **of its ratepayers repair and inspection services equivalent to those it**
523 **provides under GLCG?**

524 A. Since GLCG provides no additional repairs or inspections compared to those
525 offered for a charge by Nicor Gas, GLCG does not fulfill any *incremental* safety
526 function. Further, I reject Nicor Gas witness Erickson's assertion that it is
527 irresponsible to preclude Nicor Gas repair services provided directly to Nicor
528 Services for GLCG.

529
530 **Q. If there is no incremental safety benefit with GLCG, what benefit does**
531 **GLCG provide?**

532 A. GLGC is basically a financial product covering the cost of repairs of exposed piping.
533 Nicor Gas provides nearly all the services for GLCG, including billing, solicitation,
534 repairs and inspections. My calculations of the actuarial cost of providing GLCG
535 show that the financial benefit is miniscule compared to the risk premium.

536
537 **Q. Does Nicor Gas risk its ratepayers' safety when it neglects to aggressively**
538 **provide them information regarding its repair and inspection services?**

539 A. Nicor Gas has created a situation where ratepayers do not understand the full
540 extent of services available. Absent such knowledge, ratepayers may be less

inclined to have these inspections performed for concerns about having the gas shut off. The reduced inclination would adversely affect safety.

Q. What evidence have you found for unsafe conditions?

A. In the past, Nicor Gas informed its ratepayers about its inspection and repair services when providing safety information about appliance connectors. Witnesses Mr. O'Connor and Dr. Ros cite the *Adams v. Northern Illinois Gas Co.* decision in their rebuttal testimonies. That decision states,

The record also includes copies of "Consumer News" notices that NI-Gas sent to its customers. The August/September 1978, June/July 1980, summer/fall 1981, and December 1981 notices indicated that an old connector could crack, creating an unsafe condition, when the appliance was moved. The December 1981, January 1985, May 1986, and June 1987 notices warned: "The U.S. Consumer Product Safety Commission has warned that certain appliance connectors manufactured prior to 1968 may be unsafe. If you are concerned, do not try to move the appliance to inspect the connector. ***Instead, call a qualified service agency of NI-Gas to make the inspection.***" *Adams v. Northern Illinois Gas Co.*, 211 Ill.2d 32, 40 (2004) (emphasis added)

Tellingly, this warning to call for an inspection predates Nicor Gas' GLGC, and Nicor Gas no longer tells customers to call the utility for an inspection in its safety publications. (Nicor Gas' 2010 Safety Notice – Attachment H)

Q. Does this situation appear to be creating unsafe conditions?

567 A. Yes. It leaves customers less likely to correct important safety problems by making
568 action less available. Regardless of the reason for Nicor Gas' behavior, the
569 resulting conditions are less safe. If Nicor Gas is creating unsafe conditions in
570 order to boost its affiliate's profits, this is another important reason for the
571 Commission to deny Nicor Gas' proposed OA and approve Staff's proposed
572 modifications.

573

574 **Q. If Nicor Gas stopped supporting GLCG with repairs and inspections, would**
575 **this create a safety hazard?**

576 A. No. Ratepayers on GLCG could still have their repairs performed by Nicor Gas
577 and then pay for those repairs after the service is performed, at cost.
578 Additionally, as suggested by Nicor Gas witness Dr. Ros, Nicor Services could
579 simply reimburse its GLCG customers for those repairs. However, such a
580 product would make clear that the repair services are available without GLGC,
581 reducing its appeal.

582

583 **Q. What does the information about the safety functions of repairs and**
584 **inspections outlined by Mr. Erickson reveal about Nicor Gas' suppression**
585 **of information about its repair and inspection services?**

586 A. If the safety functions of repairs and inspections outlined by Mr. Erickson are

true, then Nicor Gas' suppression of that information demonstrates willingness to put its affiliate's profits ahead of its ratepayers' safety.

3. The market competitiveness of gas line warranty products in Nicor Gas' service territory.

Q. Have you testified that the market for gas line warranty product in Nicor Gas' service territory is not competitive?

A. Yes. The evidence that I provided in my direct testimony led me to conclude that the market for gas line warranty products in Nicor Gas' service territory is not competitive. (Staff Ex. 2.0, pp. 30-33) From 2007-2009, the average actuarial cost of these repairs is \$1.52; the remaining \$57.88 is what Mr. Ros describes as the "risk premium." (Nicor Gas Ex. 4.0, p. 16) For GLCG, the risk premium is 38 times the actuarial cost. This does not reflect a competitive price determined in a competitive market, but rather, a huge profit margin over costs as illustrated in Figure 3 – GLCG Actuarial Cost and Risk Premium.

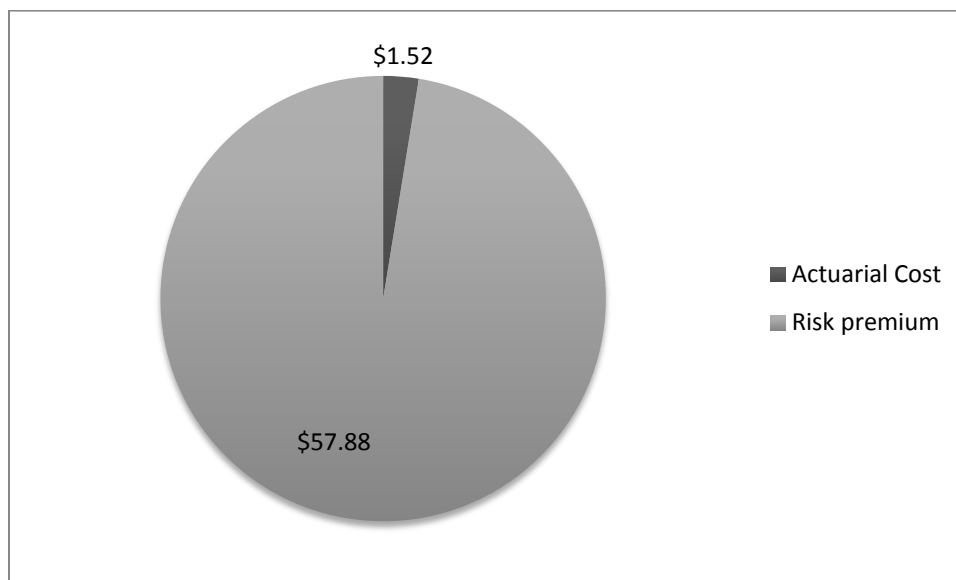


Figure 3 – GLCG Actuarial Cost and Risk Premium

Q. Are there any close substitutes in Nicor Gas' service territory?

A. No. I do not believe that there are any close substitutes in Nicor Gas' service territory because Nicor Services has a market share of 99.6%, the price elasticity of demand for GLCG is highly inelastic, and potential competitors have been driven out of the market or are not actively marketing it.

Q. Did Nicor Gas provide evidence of competitors' products within Nicor Gas' service territory in its rebuttal testimony?

613 A. Yes. Nicor Gas witness Ros notes that there are two firms providing alternate
614 products within Nicor Gas' service territory. These products are Gas Line Guard
615 provided by Santanna Energy Services ("SES") and the Utility Shield offered by the
616 Manchester Group.

617

618 **Q. Have you been able to obtain information about how many Gas Line Guard**
619 **customers SES has and its Gas Line Guard activities in Nicor Gas' service**
620 **territory?**

621 A. Yes. SES has fewer than 1000 Gas Line Guard customers in Nicor Gas' service
622 territory. SES reports that it only marketed its product to its Customer Select
623 ("CS")⁸ customers. Furthermore, SES no longer markets its Gas Line Guard
624 product in Nicor Gas' service territory because Nicor Gas refused to provide billing
625 services under the Third Party Billing Service ("TPBS") for CS. (SES responses to
626 Staff DR DAS-SES 01.01-01.05 – Attachment I)

627

⁸ Customer Select ("CS") is Nicor Gas' residential and small commercial choice program. CS operates under Riders 15 and 16 of Nicor Gas' tariff.

628 **Q. Have you been able to obtain information for Nicor Gas' service territory**
629 **about the number of Utility Shield customers and Manchester Group's**
630 **Utility Shield activities?**

631 A. In its responses to Staff DR DAS-IGS 01.01-01.05 (Attachment J), IGS, an
632 intervenor in this case, responded on behalf of its subsidiary the Manchester Group
633 that there are fewer than 1000 Utility Shield customers in Nicor Gas' service
634 territory. Similar to SES, the Manchester Group only marketed its product to its
635 Customer Select transportation customers, and it no longer markets its Utility Shield
636 product in Nicor Gas' service territory.

637

638 **Q. What is the market share of Nicor Services in the gas line warranty market**
639 **in Nicor Gas' service territory?**

640 A. A firm's market share is its percentage of customers in the relevant market. Since
641 Nicor Services had more than 449,500⁹ of the fewer than 451,500 total gas line
642 warranty customers in 2009, the market share for Nicor Services is more than
643 99.6%.

⁹ Based on Nicor Gas Ex. 4.0, p. 15, footnote 4.

644

645 **Q. Do you agree with Dr. Ros that two other suppliers in the market is**
646 **evidence of a competitive market?**

647 A. No. It does not appear that either firm constitutes a serious threat to Nicor
648 Services' market share or that their entry into this market has restrained the GLCG
649 price to a competitive level. Neither of these firms offered a product before 2006,
650 so for the first six years of GLCG, there is *no* evidence that there were *any*
651 competitors offering similar products in Nicor Gas' service territory. Furthermore,
652 Nicor Gas' well orchestrated misperception that GLGC is the means to prevent
653 shutoffs along with other advantages that Nicor Gas provides to Nicor Services
654 prevent any meaningful competition and, thus, price is not constrained to the
655 competitive level.

656

657 **Q. Do you agree with Dr. Ros that the relevant market should include "all the**
658 **options consumers have when they self insure?"**

659 A. No. The existence of more extensive warranty plans does not mean that they
660 should be included in the analysis of the relevant market. These other products are
661 not close substitutes for GLCG. An economic test for how close a substitute one
662 good is for another is the cross-price elasticity of demand. It measures how
663 sensitive the quantity demanded for one product is to price changes in the other

product. Absent proof of a close relationship, these more extensive products should not be included. Nicor Gas bears the burden of proof, and Dr. Ros has not shown that any of these other products have such a relationship. Therefore, I disagree with his assertion that self-insurance is an appropriate substitute, and do not believe that these other products should be used to analyze GLCG's market power.

Q. What other evidence do you find that counters Dr. Ros' assertion that the gas line warranty market in Nicor Gas' service territory is competitive?

A. I consider the product's responsiveness to price changes. Economists term buyers' responsiveness to a change in price the price elasticity of demand. This is the percentage change in number of customers divided by the percentage change in price. Nicor Services raised the price for GCLG twice, in 2004 from \$2.50 to \$3.95 and then again in 2007 from \$3.95 to \$4.95. I do not have sufficient data to estimate the price elasticity of demand for the 2004 price change, but I estimate it following the 2007 price change. Over the period April 2006 through February 2007, the number of GLCG customers increased by an average of [REDACTED] per month. (Nicor Gas response to Staff DR DAS 1.02 Confidential Exhibit 1) After the 25% price increase, the rate of customer growth slowed. Over the following year, instead of increasing by [REDACTED], the number of customers only increased by [REDACTED].

(Id.) The lost growth of [REDACTED] was [REDACTED] % of the number of customers before the price change. The 25% *increase* in price appears to have led to a [REDACTED] % *loss* in annual growth in customers. This implies a price elasticity of demand equal to [REDACTED] over a full year.

Q. What do you conclude from a price elasticity of demand of this magnitude?

A. Economists describe a price elasticity of demand equal to [REDACTED] as *highly* inelastic, which indicates that a change in price leads to only a very small change in quantity demanded. It is usually found for necessities and for commodities that do not have close substitutes. For example, two studies concluded that the price elasticity of demand for gasoline is about -0.25,¹⁰ which is *more* responsive to a change in price than [REDACTED].

Q. Nicor Gas witness Dr. Ros charges that you have completely ignored the

¹⁰ Elasticities of Road Traffic and Fuel Consumption with Respect to Price and Income: A Review, Phil Goodwin, Joyce Dargay and Mark Hanly, *Transport Reviews*, Vol. 24, No. 3, 275–292, May 2004
Explaining the variation in elasticity estimates of gasoline demand in the United States: A meta-analysis
Espey, Molly, Energy Journal. Vol. 17, no. 3, pp. 49-60. 1996

evidence of pricing of similar products. (Nicor Gas Ex. 4.0, p. 16) What other evidence do you find from an examination of prices of similar products?

A. Most of the other products mentioned by Dr. Ros indicate that GLCG is over-priced. Dr. Ros draws a comparison between GLCG and Peoples Gas' Pipeline Protection Plan ("PPP") and the SES' Gas Line Guard. He ignores Dominion's In Home Gas Line Repair, BSG's Guardian Care Gas Line Protection and Manchester Group's Utility Shield.

Q. What understanding is critical when evaluating the prices of these plans?

A. First, in order to do an apples-to-apples comparison, you have to understand that the actuarial cost does not rise significantly when you increase the maximum coverage from \$300 for PPP to \$600 for GLCG. This means that the price can be compared for GLCG which is \$4.95 per month and PPP which is only \$2.95 per month; the actuarial cost for PPP is effectively the same. Therefore, the risk premium charged for PPP is significantly less. Second, increasing the maximum coverage does not increase the other costs, *all of which are independent of the level of maximum coverage*. So when Dr. Ros states that "GLCG provides twice the coverage at less than twice the price" (Nicor Gas Ex. 4.0, p. 17), his statement is disingenuous because he knows that the coverage being doubled does not

double the cost and, in fact, does not significantly increase the cost. (Nicor Gas response to Staff DR DAS 18.09a)

Q. What does an apples-to-apples comparison show?

A. PPP is a good comparison because it is offered by an affiliate of Peoples Gas and supported by the LDC's services so its costs are likely to be similar. Nicor Gas spends less than \$4,000 a year on repairs that would not be covered by PPP (Attachment E) compared to a total of \$631,000 in annual repair costs. (Nicor Gas Ex. 2.0, p. 42) In other words, if Nicor Gas were to limit its coverage to \$300, the annual actuarial cost would fall from \$1.52 to \$1.51. Or conversely, if Peoples Gas were to offer a \$600 maximum coverage on PPP, its actuarial cost would rise by one cent. If we assume that, given the same degree of utility support, the actuarial cost for each product is approximately the same, then the risk premium for PPP is only \$33.89 versus the \$57.88 for GLCG. And what I call the risk premium multiple ("RPM") is 15 instead of 38. Figure 4 – Risk Premium Comparison below shows the risk premiums of several of the other products. This evidence shows that the risk premium for GLCG is excessive. It also indicates that the margin on GLCG must be *at least* equal to the difference between the two risk premiums - \$24 per customer.

Product	Monthly Price	Annual Price	Max Coverage	Actuarial Cost	Risk Premium	RPM
GLCG	\$ 4.95	\$ 59.40	\$ 600.00	\$ 1.52	\$ 57.88	38
GLG	\$ 4.95	\$ 59.40	\$ 600.00	\$ 1.52	\$ 57.88	38
FES	\$ 4.49	\$ 53.88	\$ 3,000.00	\$ 1.52	\$ 52.36	34
PPP	\$ 2.95	\$ 35.40	\$ 300.00	\$ 1.51	\$ 33.89	22
Dom	\$ 2.50	\$ 30.00	\$ 1,000.00	\$ 1.52	\$ 28.48	19
US	\$ 2.00	\$ 24.00	\$ 1,500.00	\$ 1.52	\$ 22.48	15
BSG	\$ 1.99	\$ 23.88	\$ 4,000.00	\$ 1.52	\$ 22.36	15

Figure 4 – Risk Premium Comparison

Q. What other evidence do you find that indicates that the gas line warranty market in Nicor Gas' service territory is not competitive?

A. Nicor Gas has repeatedly interfered with the "free market" to protect Nicor Services market share and profits. These actions negatively affect competition in this market. I have obtained information with respect to three firms: Progressive Energy Group, Manchester Group, and Santanna Energy Services.

Q. How has Nicor Gas interacted with Progressive Energy Group?

A. Staff provided information in its direct testimony regarding a request for services from Progressive Energy Group ("PEG") to Nicor Gas for services to support its competitive product. (Staff Ex. 2.0, pp. 37-39) Nicor Gas initially offered to provide billing services after a significant delay, but the price was discriminatory.

Eventually, Nicor Gas declined to provide any billing or solicitation services to support PEG's competitive product.

Q. Why do you say the price was discriminatory?

A. I say that the price was discriminatory because Nicor Gas offered to provide billing service to PEG at \$.025 per bill while it provided its affiliate Nicor Services the same billing service at \$0.112 per bill.

Q. How has Nicor Gas interacted with the Manchester Group?

A. The Manchester Group ("MG") is a subsidiary of IGS, so IGS provided some evidence of MG's interactions with Nicor Gas in response to Staff DR DAS-IGS-01.05b. Nicor Gas also provided some of its correspondence in Nicor Gas responses to Intervenor DR IGS 2.15 Exhibit 1-4 and Supplemental Exhibits 5-8 (I have combined these documents in chronological order in Attachment K). Manchester Group approached Nicor Gas to determine the services that Nicor Gas was willing to provide to support MG's Utility Shield product. As before, Nicor Gas offered only a discriminatory price and implementation period before declining to provide any services at all.

Q. Why do you say the price was discriminatory?

772 A. Like the offer to PEG, the offer to Manchester was at \$.025 per bill while at the
773 same time providing for its affiliate Nicor Services the same service at \$0.112 per
774 bill.

775

776 **Q. How has Nicor Gas interacted with Santanna Energy Services (“SES”)?**

777 A. SES initially included its Gas Line Guard charges to its CS customers within the
778 Third Party Billing Service (“TPBS”), as a fixed charge in the bill in a separate line
779 item. After SES had done this for at least 9 months, Nicor Gas discovered what
780 SES was doing and denied SES the right to submit such charges under this tariffed
781 service. (Nicor Gas response to Staff DR DAS 17.06 Exhibits 1 and 2 – Attachment
782 L)

783

784 **Q. How did Nicor Gas justify its refusal to bill for Gas Line Guard under**
785 **TPBS?**

786 A. Nicor Gas stated that it would only bill for “commodity-related charges.”
787 (Attachment L) That phrase does not occur in the Alternative Gas Supplier (“AGS”) Law which requires Single Billing to be offered and defines it as “the combined
788 billing of the services provided by both a natural gas utility and an alternative gas
789 supplier to any customer who has enrolled in a customer choice program.” (220
790 ILCS 5/19-105) Furthermore, Nicor Gas’ Commission-approved tariff states,
791

792 Third Party Billing Service.

793 Any third party desiring to have the Company to include its charges
794 to the customer on the Company's bill shall enter into *the*
795 *Company's standard contract that stipulates the procedures to be*
796 *followed.* The Company will provide up to six (6) standard lines of
797 text that may be used by the third party. The Company will process
798 customer payments in a timely manner and will electronically
799 forward payments to the third party's bank account and notify the
800 third party of the customer's payment on a daily basis. The fee for
801 billing and payment processing will be \$0.25 per bill. If the third
802 party would like additional services with respect to billing, the
803 Company and third party will negotiate in good faith the fees for
804 such additional services. The Company will report these additional
805 services and fees to the Illinois Commerce Commission as
806 assurance that any such additional services and fees are being
807 offered on a non-discriminatory basis.

808 On the contrary, Nicor Gas' standard TPBS contract specifically permits its
809 suppliers to bill for three charges. "The Supplier's Billing Charges shall consist of a
810 maximum of three (3) charges and descriptions to appear on the Customer's
811 regular utility bill." (Nicor Gas Consolidated Billing Services Agreement, Appendix
812 A, p. 8 – Attachment M) The contract contains no restrictions on what those
813 charges can be for.

814
815 **Q. What do you conclude from Nicor Gas' refusal to bill for Gas Line Guard**
816 **under TPBS and its interactions with potential and actual competitors?**

817 A. It appears that Nicor Gas intends to protect its affiliate's market shares in the gas
818 line warranty product by enforcing non-existent restrictions under its contracts. This
819 is not in the public interest.

820

821 **Q. Did Nicor Gas witness O'Connor argue that the AGS Law means that the**
822 **legislature meant there should be no oversight over any other markets?**

823 A. Nicor Gas witness O'Connor points to the AGS Law, which is meant to prevent the
824 extension of utility market power into the market for commodity gas supply. He
825 implies that since the Illinois General Assembly could have extended that protection
826 to other markets, but chose not to, a similar law is not needed to protect against
827 that same leverage being applied in other markets. (Nicor Gas Ex.2.0, pp. 8-9)

828

829 **Q. Do you agree with Nicor Gas witness O'Connor's conclusion regarding the**
830 **AGS Law?**

831 A. No. I disagree for two reasons. First, the absence of action does not imply tacit
832 support for this behavior. Mr. O'Connor makes the same mistake regarding the
833 Commission's Administrative Rules. The absence of a specific prohibition is not an
834 indication that additional intervention is not necessary. Second, the CS market
835 appears to be much more competitive and has less utility interference.

836

837 **Q. What evidence does the Customer Select (“CS”) program, under which**
838 **these alternative gas suppliers operate in Nicor Gas’ service territory,**
839 **provide to support increased intervention on the part of the Commission?**

840 A. The AGS Law governs utility and affiliate interaction. The AGS Law sets forth ways
841 to prevent the utility from extending its market power in distribution into the
842 commodity market. Therefore, it is instructive to consider the market structure for
843 commodity gas within Nicor Gas’ service territory in light of these requirements and
844 prohibitions. The indicators of a competitive market are seen in this market. Those
845 indicators are that there are many suppliers, the affiliate’s market share is
846 moderate, and that there is equal access to utility provided services.
847

848 **Q. How many CS suppliers are there in Nicor Gas’ service territory?**

849 A. According to Nicor Gas’ webpage about CS, there are currently 15 suppliers in the
850 CS program, one of which is Nicor Gas’ affiliate, Nicor Advanced Energy (“NAE”).
851

852 **Q. What is NAE’s market share?**

853 A. NAE is the [REDACTED] largest supplier (in terms of both number of customers and annual
854 usage) with about a [REDACTED] market share. (Nicor Gas response to Staff DR DAS 9.01
855 Confidential Ex. 2) This is a significantly different picture from the market for gas

line warranty products within Nicor Gas' service territory in which the Nicor Gas affiliate Nicor Services has a 99.7% market share.

Q. What do the Commission's Administrative rules require and prohibit with regard to utility and affiliate interaction?

A. Nicor Gas is prevented from directly providing certain services such as solicitation and prohibits any preferential treatment in the provision of services under the CS program.¹¹

Q. Does Nicor Gas' solicitation on behalf of Nicor Services allow Nicor to effectively sidestep this prohibition?

A. Yes. Nicor Gas cannot directly solicit on behalf of NAE. However, nothing prevents Nicor Gas from soliciting for Nicor Services and then having Nicor Services solicit its own customers on behalf of NAE. (Nicor Gas response to Staff

¹¹ TITLE 83: PUBLIC UTILITIES -CHAPTER I: ILLINOIS COMMERCE COMMISSION
SUBCHAPTER d: GAS UTILITIES
PART 550 NON-DISCRIMINATION IN AFFILIATE TRANSACTIONS FOR GAS UTILITIES
SECTION 550.30 MARKETING AND ADVERTISING

DR DAS 11.01) Incidentally, a fifth of Nicor Gas residential customers are on GLCG. (Staff Ex. 2.0, p. 19) This allows NAE and other affiliates access to a prime market created by Nicor Gas that other suppliers cannot access.

Q. Do you have any evidence that suggests to you that Nicor Services solicits its GLCG customers on behalf of NAE and Nicor Solutions, both Nicor Gas affiliates?

A. Yes. More than 4.0% (18,200 - Nicor Gas response to Staff DR DAS 11.02) of 449,778 GLCG customers are NAE CS customers. Less than [REDACTED] ([REDACTED] - Nicor Gas response to Staff DR DAS 9.01 Confidential Ex. 2) of the 2,147,150 customers eligible for CS are NAE customers. Therefore, GLCG customers are more than [REDACTED] as likely to be customers of NAE than eligible customers overall.

Q. What do you conclude about the parallels between these related markets?

A. It is my opinion that Nicor Services' market share reflects the lack of those consumer protections that have been established in the CS market and it is appropriate and reasonable for the Commission to act to provide similar consumer protections to the extent allowed under the Public Utilities Act for the other products offered by Nicor Gas affiliates.

890 **Q. What is the theory of contestable markets?**

891 A. The theory of contestable markets posits that, under certain conditions, the
892 continuous threat of entry into a market by competitors is sufficient to prevent
893 existing incumbent firms (even a monopoly) from raising prices high enough to earn
894 supra-normal profits (i.e., profits above the level expected in a more obviously
895 competitive market). According to Dr. Ros, necessary conditions to support this
896 theory are “that firms have access to the same technology, that there are zero sunk
897 costs, and that the entry lag is less than the price adjustment lag for existing firms.”
898 (Nicor Gas response to Staff DR DAS 18.17 – Attachment N) For this reason, the
899 applicability of contestable market theory to real-world markets is limited.

900

901 **Q. What does Dr. Ros conclude about the applicability of contestable market**
902 **theory to the GLCG market dominated by Nicor Services?**

903 A. While Dr. Ros admits that contestable market theory is not the dominant economic
904 theory on market organization (Nicor Gas response to Staff DR DAS 18.17 –
905 Attachment N), he nevertheless concludes that the price of GLCG is set at a
906 competitive level, due to the market being contestable. (Nicor Gas Ex. 4.0, p. 31)

907

908 **Q. Do you concur with Dr. Ros’ assessment?**

909 A. No. Dr. Ros has not established the lack of material barriers to entry in this market,
910 and he has not identified any firms that pose a viable threat. Otherwise stated, he
911 has not shown that the theory of contestable markets applies in this instance. None
912 of Dr. Ros' three necessary conditions seems likely to hold in this case; thus, this
913 theory is misapplied to the instant case. It is clear that since only Nicor Services
914 has access to the most cost effective billing service and repairs service and the
915 irreplaceable mover calls solicitation, the requirement for access to the same
916 technology does not hold. Second, Dr. Ros assumes away all sunk costs but it is
917 likely that the cost of moving into a market is much higher than he alleges. Lastly,
918 Nicor Services could lower its prices at any time while the entry lag for these firms
919 is significant.¹²

920
921 **Q. What else did Dr. Ros argue regarding options that restrain the price that**
922 **Nicor Services can offer?**

¹² Especially considering that Nicor Gas was telling them that it would take 8 months to set up a billing system. (Attachment K)

923 A. Another reason that Dr. Ros gives for Nicor Services only being able to charge a
924 competitive price is that he claims self-insurance is the option that most ratepayers
925 choose. As I discussed above about the argument regarding potential competition,
926 Dr. Ros takes an economic theory and misapplies it here to the instant case
927 because customers are not aware of their actual options as shown below.

928
929 **Q. When ratepayers are given the choice to sign up for GLCG, how likely is it**
930 **that they are aware that Nicor Gas provides repairs and inspections under**
931 **Customer Care Services?**

932 A. It is very unlikely that customers are aware of the alternatives. Nicor Gas does not
933 generally notify its customers that it provides this service. In fact, Nicor Gas claims
934 that it only notifies customers during a gas leak field visit (Nicor Gas corrected
935 response to Staff DR DAS 3.03 – Attachment O) or during a gas leak emergency
936 call (Nicor Gas response to Staff DR DAS 16.03 – Attachment P). However, there
937 is no mention of these repair services in the gas leak materials provided by Nicor
938 Gas in this case. Rather, those customers are instead solicited for GLCG after
939 being told that Nicor Gas is not obligated to fix leaks on the customer's pipes. (Nicor
940 Gas response to Intervenor DR IGS 2.18 Exhibit 2 – Attachment Q)

941
942 **Q. Do CS suppliers appear to be aware of the availability of these repair**

943 **services?**

944 A. No. Nicor Gas witness O'Connor cites this as the "most obvious option" for
945 suppliers, but suppliers are unaware of the availability of this option. (Nicor Gas Ex.
946 2.0, p. 46) Even when queried by suppliers about what services are available to
947 support warranty products, Nicor Gas declines to provide this information.
948 (Attachment K) The resulting asymmetric information protects GLCG offered by
949 Nicor Services. Nicor Gas' scripts give the impression that the ratepayer now has
950 complete information about the *limits of what Nicor Gas offers*. It does this by
951 telling ratepayers about *the limits of Nicor Gas's obligation*.

952

953 **Q. Do the rebuttal scripts used by Nicor Gas solicitors after potential**
954 **customers decline to make a decision on the service pressure the**
955 **ratepayers to make immediate decisions about GLCG?**

956 A. Yes. Despite the fact that Nicor Gas witness Ros allocates the responsibility for
957 finding the relevant information about their options on the ratepayers. (Nicor Gas
958 Ex. 4.0, p. 13) Both Nicor Gas and Nicor Services pressure ratepayers during the

solicitation process to hinder the ratepayers' ability to consider information about their options. (Staff Ex. 2.0 Attachment G, pp. 1-2)¹³ It appears that Nicor Gas has no interest in ratepayers gaining access to the information they need to make informed decisions. This is another example of how Nicor Gas uses its position as the utility to leverage profits for its affiliate and thus ensuring incentives for its decision makers.

Q. Nicor Gas maintains that GLCG's low complaint rate indicates that customers are satisfied with GLCG. Do you agree?

A. No. It might be that the customers are blissfully unaware of their options. Since Nicor Gas never informs GLCG customers about these alternative services even when they are reporting a gas leak or during the subsequent services call, GLCG

¹³ GLCG Rebuttals "I Need to Talk to My Spouse/I need to think about it."

"I can appreciate that--and obviously you want to make an educated decision. Let me suggest this: Since I already have you on the line, Mr/Ms [], I can go ahead and get your coverage set up for you today. You will then receive a welcome packet in the mail in about 5 to 10 business days. Your Welcome Packet clearly outlines all the terms, conditions and benefits of the program, which you can then review in the comfort of your home (with your spouse). Now, Mr/Ms [] we are so confident you are going to like this program, that if for any reason you feel it's not quite right for you, and you have not had service, all you need to do is give us a call back and as long as you have not had service, you can simply cancel without any further cost or obligation except for your time on the plan.. Does that sound reasonable?"

971 customers never discover this critical piece of information that would influence their
972 decision between identical utility or affiliate services. Absent the suppressed
973 information, they have no reason to complain, because they never perceive that the
974 utility service is an option. It is certainly possible that GLCG customers would still
975 prefer to stay with GLCG after being presented with the option of receiving the
976 same service directly from the utility at a fixed cost. Nevertheless, as it stands now,
977 all the options are not being fully disclosed to the customers for them to make the
978 best informed decisions themselves; instead, GLCG is aggressively solicited,
979 leaving customers to feel like they have no choice but to sign up for GLCG or to
980 remain on GLCG.

981
982 **Q. Does the literature cited by Dr. Ros provide any insight into the need for**
983 **better information?**

984 A. Yes. The literature acknowledges that the efficiency of insurance decisions
985 depends on the access to “loss information,” which is information about the
986 probability and size of the potential loss. Absent this information, the literature
987 indicates that the self-insurance decisions will not be efficient. (OECD Policy
988 Roundtable (1998), “Competition and Related Regulation Issues in the Insurance
989 Industry,” pp. 22-23) While Nicor Gas has this information and certainly makes it

available to Nicor Services, it is not willing to provide it to ratepayers or competitive suppliers.

Q. Is the self-insurance decision here efficient?

A. No. Customers are unlikely to have a good grasp on either the probability or size of the potential loss and because of advantages given to the affiliate by the utility, price competition is not likely to drive the price of the insurance toward the expected loss. More importantly, the Nicor-orchestrated misinformation about the ability to avoid shutoffs with leaks without GLGC causes them to have an inflated view of the value of GLGC. Thus, ratepayers do not develop an accurate picture of their options.

Q. Nicor Gas witness Dr. Ros maintains that Commission interference in a competitive market will reduce the incentive to innovate leading to lost efficiency for ratepayers. (Nicor Gas Ex. 4.0, p. 20) Do you agree?

A. No. Nicor Gas' inputs are unique. Competitors don't get access to them. Customers are not aware of them. Innovation and the resulting product differentiation that separates GLCG from both Gas Line Guard and Utility Shield result from Nicor Gas' legal obligations to provide utility service, not innovation by Nicor Services. I see three "innovations": 1) single billing, 2) instant repairs and 3)

1010 head of the line, mover call solicitations. Together these innovations create an
1011 undeserved affiliate preference.

1012

1013 **Q. Nicor Gas witness Dr. Ros implies that billing options for having Nicor Gas**
1014 **repair for the customers directly and having the supplier simply**
1015 **reimbursing the customer are equivalent. Do you agree?**

1016 A. No. I do not believe that customers would view the two as equivalent. The single-
1017 billing option has three advantages. It is more convenient and does not put the
1018 customers at risk of default by their supplier. Also, if the customer is liquidity
1019 constrained, paying for a significant repair may be a burden and discourage
1020 enrollment in such a product. Significantly, SES states that it does not believe that
1021 such an option would make its product inferior to GLCG. (Attachment I)
1022 Additionally, Dr. Ros admits that all other things being equal, customers prefer
1023 more convenient options. (Nicor Gas response to Staff DR DAS 18.07b)

1024

1025 **Q. Does Nicor Services' exclusive single billing convenience result from**
1026 **innovation or Nicor Gas' obligation to provide a utility bill to its ratepayers?**

1027 A. The advantage that Nicor Services derives from single billing stems from Nicor Gas'
1028 obligation to provide a utility bill to its ratepayers. Nicor Gas passes the gains from
1029 economies of scale on to its affiliate.

1030

1031 **Q. Does Nicor Gas interfere with the unregulated market by preventing**
1032 **unaffiliated competitors from using its single-billing feature?**

1033 A. Yes. Nicor Gas has repeatedly made discriminatory offers to potential competitors,
1034 refusing to bill for non-commodity products under TPBS and refusing to provide
1035 billing for any non-commodity products to any non-affiliate.

1036

1037 **Q. Does Nicor Services' advantage in instant repair convenience result from**
1038 **innovation or Nicor Gas' obligation to respond to gas leaks?**

1039 A. Nicor Services' exclusive instant repair convenience results from Nicor Gas'
1040 policy to provide gas leak repair services to its customers.

1041

1042 **Q. Has Nicor Gas participated in Nicor Inc.'s "well orchestrated misperception**
1043 **that GLGC is the means to prevent shutoffs"?**

1044 A. Yes. Nicor Gas has not made customers generally aware that it will repair gas
1045 leaks on customer's pipes even though such knowledge would increase safety.
1046 Nicor Gas has allowed its customer service people to say Nicor Gas is not required
1047 to fix leaks and has allowed Nicor Services' call center personnel to say the same
1048 thing.

1049

1050 **Q. Nicor Gas witness Dr. Ros addresses your concern about Nicor Services**
1051 **having access to Nicor Gas' mover calls. Do you agree?**

1052 A. Yes. He implies that other solicitation channels are equivalent. I disagree. Other
1053 solicitation channels do not replicate the first service that Nicor Services receives.
1054 Customers moving are likely to be unfamiliar with gas pipe history of their new
1055 location and are most likely to purchase GLCG with the mover call. (Nicor Gas Ex.
1056 4.0, p. 12)

1057
1058 **Q. Does Nicor Services' exclusive mover call solicitation result from**
1059 **innovation or Nicor Gas' obligation to sign up ratepayers for utility service?**

1060 A. Nicor Services' exclusive mover call solicitation results from Nicor Gas' obligation to
1061 sign up ratepayers for utility service and its preferential treatment of its affiliate with
1062 respect to the price for single billing.

1063
1064 **Q. Has Nicor Gas interfered with the competitive market by preventing other**
1065 **competitors soliciting mover calls?**

1066 A. Yes. Nicor Gas has repeatedly interfered with the market itself by refusing to
1067 provide any solicitation opportunities for non-affiliates.

1068
1069 **Q. What do you conclude about Nicor Services' "innovation" and its**

**protection by Nicor Gas? Do you have an opinion on a reasonable
response by the Commission?**

A. Unique GLCG features do not result from innovation by Nicor Services but rather from Nicor Gas' position as a utility service provider. These innovations should not be protected as Dr. Ros advocates but rather they should be serving ratepayers, not shareholders. Nicor Gas' actions to interfere in this market for gas line warranty products reduce competition in the market and, as such, are not in the public interest. Therefore, these actions should be prohibited by the Commission.

4. Nicor Gas' Cost Support for GLCG.

Q. Did Nicor Gas provide for the record any specific cost support for GLCG?

A. No. While its affiliate, Nicor Services, must have access to detailed cost information about GLCG costs, but it has declined to provide it to Nicor Gas. If it were in Nicor Services' best interests to provide such data, it would do so here. The absence of this data suggests that this data cannot justify the margins shown in my direct testimony.

Q. Nicor Gas witness O'Connor states that there is an error in how the 10k profits were calculated. Please respond.

A. The 10k profit calculations performed in Figure 8 of my direct testimony (Staff Ex.

2.0, pp. 45-46) were initially calculated using Nicor Inc.'s 2008 10k. This document does not breakdown Nicor Inc.'s Other Energy Ventures ("OEV") data into "Wholesale Marketing" and "Other" portions. My calculations accurately used the information contained in that 10k. When the data from the 2009 10k became available, I updated my analysis. The analysis in my direct testimony correctly reflects the *before-tax* profits from Nicor Inc.'s OEV for 2008 and 2009. Mr. O'Connor's testimony breaks down the data into "Wholesale Marketing" and "Other" portions of OEV using specificity that only became available in the 2009 10k. This new data does not make my earlier calculations incorrect.

Q. Nicor Gas witness O'Connor states that the wrong average tax rate was used to calculate profits. Is that correct?

A. Perhaps. In my direct testimony, I attempted to demonstrate fairly the level of taxes shown in the 10k and as such I used the average tax rate from the 10k. I am willing to accept the tax rates used by Mr. O'Connor. (Nicor Gas Ex 2.13 and its response to Staff DR DAS 22.01 Exhibit 1) I have provided revisions to certain calculations from my direct testimony in Figure 5 – Corrections to Staff Ex. 2.0 Numerical Analysis. However, changing that tax rate would not change my conclusions or recommendations.

Corrections to Staff Ex. 2.0 Numerical Analysis						
Page	Line	Figure	Row / Amount	2007	2008	2009
40		4	Annual Revenue per customer	\$57.40 ¹⁴		
40		4	Estimated GLCG Revenues	\$22,080,862		
44	986		"effective tax rate"			38.73%
44	987		"final minimum net income"			\$14.9 million
45		7	Estimated GLCG Income (before tax profits)	\$20,773,610	\$23,283,097	\$24,438,453
45		7	Effective Tax Rate	39.70%	38.80%	38.73%
45		7	Estimated GLCG Net Income (profits)	\$12,526,177	\$14,249,256	\$14,974,542
45	993		"profits"			\$14.9 million
45	993		"% of the less than \$1.8 million costs"			800%
45	995		"markup"			eight-fold
45	999		"profits"			\$14.9 million
45	1000		"% of Nicor Inc. Net Income"			11%
46		8	GLCG % of Nicor Inc Net Income	9%	12%	11%
46		8	GLCG profits as a percent of costs (markup)	958%	932%	854%
50	1101		"benefit % of net revenues"			7%
50	1101		"net revenues"			\$14.9 million
57	1284		"after tas revenues"			\$10.7 million
57	1285		"% markup"			166%
57	1286		"markup"			\$14 million

Figure 5 – Corrections to Staff Ex. 2.0 Numerical Analysis

Q. Nicor Gas witness O'Connor states that since the profits for the "Other"

¹⁴ This number was changed from \$59.40 to reflect the price change from \$3.95 per month to \$4.95 per month which occurred on March 1, 2007. (Nicor Gas response to Staff DR DAS 7.01)

1112 **portion of OEV is 7%, then GLCG cannot have the profit margin that you**
1113 **estimated. Is that an accurate conclusion?**

1114 A. No. GLCG is just one of the 77 products and packages offered by Nicor
1115 Services. (Nicor Gas response to Staff DR DLH 2.02 Exhibit 13 Corrected Exhibit
1116 A – Attachment R) Also, Nicor Services offers GLCG and other products in at
1117 least seven other states. (Nicor Gas Ex. 4.2) Additionally, Nicor Services may
1118 have incurred significant startup costs from its national expansion that offset the
1119 margins received on GLCG. Furthermore, those OEV numbers also include
1120 profits and losses from both Nicor Solutions and Nicor Advanced Energy. As
1121 such there may be many costs included in the margin for OEV that are not
1122 reflective of the costs of GLGC in Nicor Gas' service territory. My analysis only
1123 addressed the known costs associated with the provision of GLCG to Nicor Gas
1124 ratepayers. There is no evidence of any other actual costs. I cannot invent
1125 these amounts and include them in my analysis. Nicor Gas, though it could
1126 provide these costs, has systematically declined to do so.

1127

1128 **Q. Are there other inconsistencies in Nicor Gas' rebuttal testimony?**

1129 A. Yes. Another inconsistency in Nicor Gas' rebuttal testimony arises between the
1130 claim that services in support of GLCG benefit ratepayers and the claim that
1131 providing such services to non-affiliates would also be harmful to ratepayers. It is

1132 not logical that providing the same service to an affiliate and a non-affiliate at the
1133 same price would have different effects on ratepayers.

1134

1135 **GLCG Conclusions and Recommendations**

1136 **Q. What do you conclude with regard to GLCG?**

1137 A. I continue to conclude that Nicor Gas and Nicor Services mislead customers into
1138 wrongly thinking that GLCG is necessary to prevent customers from being shutoff
1139 as a result of failures in exposed piping. The use of Nicor Gas' service personnel to
1140 investigate leaks and to simultaneously provide repairs allows Nicor Services to
1141 ensure the customer repair is done without shutoff. The agreement to allow Nicor
1142 Services the right to market to Nicor Gas' new and existing customers gives Nicor
1143 Services access to customers especially susceptible to inside piping failure
1144 concerns. Nicor Gas provided resources allow Nicor Services to provide GLCG at
1145 a much higher price than Nicor Gas would be allowed to charge for the same
1146 service. Nicor Gas provided resources also give Nicor Services anti-competitive
1147 market power in providing the GLCG product.

1148

1149 **Q. What are your recommendations with respect to GLCG?**

1150 A. Based on my conclusions, it is not in the public interest for Nicor Gas to provide the
1151 resources to allow Nicor Services to offer GLCG, and Nicor Gas should be

1152 precluded from doing so. Therefore, I make the following five recommendations
1153 related to GLCG:
1154 **Recommendation 2: Change Nicor Gas' OA to preclude customer solicitation.**
1155 **Recommendation 3: Require Nicor Gas to provide factual information**
1156 **regarding its currently available repair services.**
1157 **Recommendation 4: Change Nicor Gas' OA to preclude operational services**
1158 **other than those specifically authorized.**
1159 **Recommendation 5: Change Nicor Gas' OA to require that *any* Nicor Gas**
1160 **service, excluding "corporate support,"¹⁵ that supports *any* affiliate product**
1161 **that is offered to Nicor Gas ratepayers be provided to non-affiliates on a non-**
1162 **discriminatory basis.**

¹⁵ "Corporate support" means corporate oversight and governance involving administrative services (including travel administration, security, printing, graphics, custodial services, secretarial support, mail services, and records management), financial management services (including accounting, treasury, internal audit, tax, and financial reporting and planning), data processing, shareholder services, human resources, employee benefits, regulatory affairs, legal services, lobbying, and non-marketing research and development activities. Corporate support also includes strategic planning. (TITLE 83: PUBLIC UTILITIES, CHAPTER I: ILLINOIS COMMERCE COMMISSION, SUBCHAPTER d: GAS UTILITIES, PART 550 NON-DISCRIMINATION IN AFFILIATE TRANSACTIONS FOR GAS UTILITIES, Section 550.10 Definitions)

1163 Finally, the services must be priced consistently with Staff witness Hathhorn's
1164 Recommendations 1 through 3.

1165

1166 **V. Website**

1167 **Issues/Concerns**

1168 **Q What are your issues and concerns with regard to the website?**

1169 A I have the following concerns. I do not think that it serves the public interest for
1170 Nicor Gas' webpages to be out from under the jurisdiction of the Commission.

1171 Also, Nicor Inc. is unwilling to allow potential competitors to solicit customers on its
1172 website.

1173

1174 **1. Nicor Gas' webpages and Commission Jurisdiction.**

1175 **Q. According to Nicor Gas, does the Commission have oversight of the Nicor**
1176 **Inc. website?**

1177 A. Not in its own opinion. Mr. O'Connor states, "Nicor Inc. is not a public utility, and it
1178 is my understanding that the operation of its website is not subject to the
1179 Commission's jurisdiction." (Nicor Gas Ex. 2.0, p. 71)

1180

1181 **Q. Is it in the public interest for one of the primary interfaces with ratepayers**
1182 **to be beyond the Commission's control?**

1183 A. No. Nicor Gas' webpage is an important medium by which the utility interacts with
1184 its customers. The public interest is best served by Nicor Gas having its own
1185 website subject to regulation by the Commission.

1186

1187 **Q. Does the fact that other utilities have the same website structure mean that**
1188 **Nicor Gas should be allowed to continue its course?**

1189 A. No. Nicor Gas has shown that it cannot be trusted to protect its ratepayers from
1190 Nicor Inc.'s own self interests. Given this poor track record I, think it is appropriate
1191 to take steps with Nicor Gas that have not yet been taken with other Illinois utilities.

1192

1193 **2. Solicitation by potential competitors on Nicor Inc.'s website.**

1194 **Q. Have other suppliers requested that Nicor Gas provide equal rights to**
1195 **solicitation on the webpage?**

1196 A. Yes. PEG asked to use the webpage to solicit for its warranty product and other
1197 services in the same manner as Nicor Services. (Staff Ex. 2.0, Attachment M)
1198 Additionally, Dominion witness Mr. Crist has asked to Commission to require Nicor
1199 Gas to allow non-affiliates to solicit through the webpage. He states, "Nicor Gas
1200 should post links to non-affiliated marketers that will enable customers to
1201 conveniently go to the marketer's website and review products and services." (DRI

1202 Ex. 1.0, p. 10) Mr. Crist is essentially asking for equal access to Nicor Gas
1203 provided solicitation, which is consistent with my Recommendation 5.

1204

1205 **Q. How did Nicor Gas respond to this recommendation?**

1206 A. According to Nicor Gas witness O'Connor, the operation of Nicor Inc.'s website is
1207 not subject to the jurisdiction of the Commission. (Nicor Gas Ex. 2.0, p. 71)

1208

1209 **Website Conclusions and Recommendations**

1210 **Q. What do you conclude with regard to Nicor Inc.'s website?**

1211 A. Nicor Gas should be precluded from using Nicor Inc.'s website to host a Nicor Gas
1212 webpage. Recommendation 2 discussed above would preclude this. Because the
1213 affiliates and their products are also featured in this site, it creates fairness issues
1214 for any potential competitors and fosters confusion among Nicor Gas customers.
1215 Regardless of the Commission's decision regarding solicitation above, solicitation
1216 through the website is a bad idea. If it is allowed, Nicor Services should pay Nicor
1217 Gas for the market value of this solicitation per Ms. Hathhorn's Recommendation 3
1218 and it should be provided to non-affiliates in a nondiscriminatory basis, as required
1219 by my Recommendation 5. Because the products offered by third-parties (including
1220 affiliates) may not be "properly priced," it is imperative for clear disclaimers that
1221 require an affirmative customer response to be used whenever the customer goes

1222 to a third-party site (including affiliate) or to Nicor Inc.'s site. Therefore, I have the
1223 following recommendation and recommend the following language changes to the
1224 OA:

1225 **Recommendation 6: Change Nicor Gas' OA to preclude website hosting of**
1226 **Nicor Gas by any affiliate.**

1227

1228 **VI. Billing Services**

1229 **Issues/Concerns**

1230 **Q. What concerns did you raise in your direct testimony with regard to Nicor**
1231 **Gas' billing services?**

1232 A. I raised two specific concerns. First, that Nicor Gas' offer for billing services to PEG
1233 was discriminatory at a higher price than was charged to Nicor Services, and
1234 second, the billing service to Nicor Services should be provided pursuant to TPBS.

1235

1236 **Q. How did Nicor Gas respond to your concerns about Nicor Gas' billing**
1237 **services?**

1238 A. Nicor Gas witness O'Connor did not respond to the evidence provided about the
1239 discriminatory nature of the offer to PEG except to say that it was subsequently
1240 withdrawn and so it no longer needed to be considered. Nicor Gas has determined

1241 it will no longer offer any non-affiliate billing service besides TPBS. (Nicor Gas
1242 response to Staff DR DAS 1.11)

1243

1244 **Q. How do you respond to Nicor Gas' rebuttal of your concerns?**

1245 A. Nicor Gas is no longer discriminating against other suppliers because it is no longer
1246 willing to perform any non-commodity billing for non-affiliates. Now Nicor Gas
1247 discriminates not on price but access. It will not provide those services equally to
1248 all.

1249

1250 **Q. Were the Nicor Services billing services provided to any other party?**

1251 A. No. Nicor Gas argued that "the evidence demonstrates that the billing service
1252 offered to Nicor Services is not 'provided for sale to the general public' by Nicor
1253 Gas..." (Nicor Gas Initial Brief, Docket No. 08-0363, p. 131) This may have been
1254 true at the time, but it had offered this same service *twice* in the previous year at the
1255 same price as TPBS. In its response to Staff DR DAS 2.14 Exhibit 3 (Staff Ex. 2.0,
1256 Attachment L), Nicor Gas revealed that in July 2008 it was willing to provide PEG
1257 access to the same billing service used by Nicor Services. Furthermore, in its
1258 Attachment K, Nicor Gas revealed that in March 2008, it was willing to provide
1259 Manchester Group access to that same billing service. Nicor Gas was also

1260 unknowingly providing SES with the access until it discovered that SES' charge
1261 included a warranty product.

1262
1263 **Q. Does Nicor Gas distinguish between billing for commodity versus non-**
1264 **commodity products?**

1265 A. Yes. Nicor Gas maintains that TPBS and the billing services provided for Nicor
1266 Services are inherently different because one is for non-commodity service and
1267 the other is for commodity products only. "The per item billed charge for the
1268 Nicor Services billing service allows more than one *non-commodity* product to be
1269 billed. The TPBS is used for commodity based service, and does not involve
1270 charges for multiple products." (Attachment L) Nicor Gas alerted SES that Nicor
1271 Gas would no longer charge SES' customers for non-commodity products. (Id.)

1272
1273 **Q. What reason did Nicor Gas provide for refusing to bill for non-commodity**
1274 **products?**

1275 A. Nicor Gas states that it would only bill for "commodity-related charges." Of
1276 course, as shown above on pages 42-44, neither the AGS Law nor the
1277 Commission-approved tariff for this service nor the standard contract referenced
1278 therein distinguish between the two types of products. In fact, the standard
1279 contract allows for up to three charges to be included on the bill. (Attachment M)

1280

1281 **Q. Has Nicor Gas in this case shown such a set of charges?**

1282 A. Yes. Attachment L includes a list of such charges.

1283

1284 **Q. When Nicor Gas began billing on behalf of Nicor Services, did it provide**
1285 **any billing services to any other third party?**

1286 A. Apparently not. So it was not possible to determine if Nicor Gas was discriminating
1287 against non-affiliated suppliers.

1288

1289 **Q. Now that Nicor Gas provides billing services to other third parties, should**
1290 **all parties be billed under the same system?**

1291 A. Yes. It is in the public interest to subject all billing services to the same set of rules
1292 and public disclosure and to bill them all under TPBS. Nicor Gas should not be
1293 allowed to support its unregulated affiliate in a discriminatory manner.

1294

1295 **Q What is Staff's conclusion regarding Nicor Gas' discrimination in this case?**

1296 A Staff recommends that Nicor Gas be ordered to cease providing preferential billing
1297 services to its affiliates.

1298

1299 **Q. What was Nicor Gas' response to your proposal that the billing service to**
1300 **Nicor Services should be provided pursuant to TPBS?**

1301 A. Nicor Gas witness O'Connor contested my proposal to charge Nicor Services under
1302 the TPBS tariff. He objected to my testimony that the evidence provided in the last
1303 case was incomplete and that we should provide new evidence which the
1304 Commission needs to evaluate in this case. He stated that the issue had already
1305 been litigated and the Commission made its decision based on the "critical facts"
1306 provided by the Company regarding the differences of the billing services provided
1307 under TPBS and that provided to Nicor Services. (Nicor Gas Ex. 2.0, pp. 73-74)

1308

1309 **Q What does Mr. O'Connor claim are the "critical facts"?**

1310 A Nicor Gas witness O'Connor states that the critical facts are the differences in the
1311 nature of the services, the charges and the prices of the two billing services being
1312 provided. Staff has already provided evidence in its direct testimony that
1313 contradicts these alleged "facts" provided by the Company in its last rate case.
1314 (Staff Ex. 2.0, pp. 71-73) Nicor Gas should not be allowed to limit the set of facts
1315 for the Commission to consider here. Moreover, the Commission should have all
1316 the facts necessary to properly examine the OA and to determine whether the OA
1317 in the best interest of ratepayers.

1318

1319 **Q. Did Nicor Gas present evidence in its last rate case to show that the two**
1320 **billing services are not the same?**

1321 A. No. The Company only stated that such was the case. (Nicor Gas Exhibit. 45.0,
1322 Docket No. 08-0363, p. 10)

1323

1324 **Q. Do you agree with Nicor Gas witness O'Connor that the two billing services**
1325 **are different?**

1326 A. No. Based on Nicor Gas' responses to Staff discovery in this case, the two billing
1327 services are "essentially" the same.

1328

1329 **Q. How many billing systems does Nicor Gas have?**

1330 A. Nicor Gas has one billing system called the Customer Care and Billing System
1331 ("CC&B"). According to Nicor Gas, the primary physical components are servers.
1332 The servers providing billing services to Nicor Services are not used exclusively for
1333 that service. Neither are the servers used to support TPBS used exclusively for
1334 TPBS. The system also contains printers which print all bills regardless of whether
1335 TPBS or Nicor Services charges are on them. (Nicor Gas response to Staff DR
1336 DAS 10.13 – Attachment S)

1337

1338 **Q. What ancillary services does Nicor Gas provide to both Nicor Services and**
1339 **TPBS?**

1340 A. Nicor Gas states that separate modules within CC&B perform the same ancillary
1341 services for each billing service: enrollments, effective dates, drops, eligibility
1342 checks and bill messages. (Attachment S)

1343

1344 **Q. Do suppliers provide the same information as Nicor Services?**

1345 A. Yes. In Attachment S, Nicor Gas shows that most of the information provided by
1346 Nicor Services is essentially the same as suppliers under TPBS. Specifically, both
1347 will provide the individual charges for each account.

1348

1349 **Q. Are the printed bills' appearances nearly identical?**

1350 A. Yes. In Attachment S, Nicor Gas shows that Nicor Services' bills are nearly
1351 identical to bills from suppliers purchasing TPBS. The only visible difference is the
1352 marginally dissimilar amount of space allotted to each service.

1353

1354 **Q. In Docket No. 08-0363, did Nicor Gas misrepresent its billing services?**

1355 A. Yes. Nicor Gas witness Gorenz misrepresented the billing services provided by
1356 Nicor Gas when he stated, "Nicor Gas does not provide a billing service for any
1357 third party "that *is at all similar* to the billing service it provides for Nicor Services'

HVAC business.” (Nicor Gas Ex. 45.0, Docket No. 08-0363, p. 10) Based on the evidence provided here, these two services are *very* similar.

Q. How did Nicor Gas propose to allocate costs to TPBS suppliers?

A. In Docket No. 00-0620, Nicor Gas claimed that it had proposed to use the same methodology that it alleged was used to allocate costs to affiliates. (Harms Rebuttal Testimony, Docket No. 00-0620, Nicor Rehearing Ex. 2, p. 23)

Q. Did Nicor Gas’ proposal actually use the exact same method with TPBS that is used with Nicor Services?

A. No. When Nicor Gas applies fully distributed costs to the allocation, it uses two factors. The basket of costs determines the total costs to be allocated, and an allocator is applied to the basket. Nicor Gas proposed to use the same *basket* of costs for Nicor Services billing service and TPBS. However, for the *allocator* for Nicor Services, Nicor Gas chose to use 7%, which was based on a cost causation methodology as stated in the OA. The result yielded a charge equal to only \$.037 per item. (Nicor Services Billing Service Cost Studies – Attachment T) What Nicor Gas did not point out was that it proposed to allocate 50%, rather than the 7% it used for Nicor Services, of the same basket of costs, which yielded a FDC charge equal to \$.29 per bill for TPBS suppliers. (Third Party Billing Service Cost Studies –

1378 Attachment U) The difference between these results shows that either Nicor
1379 Services has gotten a really good deal or TPBS suppliers were being discriminated
1380 against.¹⁶

1381

1382 **Billing Services Conclusions and Recommendations**

1383 **Q. What do you conclude with regard to the billing services provided by Nicor**
1384 **Gas to third parties?**

1385 **A. Recommendation 7: Require Nicor Gas to charge any affiliate the same**
1386 **charge as other third parties under the Third Party Billing Service.**

1387 **Recommendation 8:** Require Nicor Gas to allow any Customer Select supplier to
1388 include non-commodity charges under the Third Party Billing Service. This last
1389 recommendation is new for my rebuttal testimony because when I asked Nicor Gas
1390 to provide any correspondence with any potential marketers regarding the provision
1391 of billing services for both commodity and non-commodity products, Nicor Gas
1392 claimed that “no such request has been received.” (Nicor Gas response to Staff DR

¹⁶ The current charge for TPBS does not include those FDC because the Commission did not see fit to recover these FDC between rate cases. So it ordered that only incremental charges be included. However, Nicor Services is still charged using the discounted FDC methodology.

1393 DAS 1.13) Nicor Gas provided three sets of correspondence subsequent to that
1394 statement. (Staff Ex. 2.0, Attachments K-N; Attachment L; Attachment K) The
1395 evidence regarding the discriminatory use of the TPBS charges with SES only
1396 came to light after the filing of my direct testimony. (Attachment L)

1397 **Q. Does this conclude your prepared rebuttal testimony?**

1398 **A.** Yes.